

31 October 2014

Civil Aviation Act and Airport Authorities Act Review
Ministry of Transport
PO Box 3175
Wellington 6140
NEW ZEALAND

Dear Sir/Madam

**Submission to the Review of the Civil Aviation Act 1990 and
Airport Authorities Act 1966**

The Virgin Australia Group of Airlines (Virgin Australia) welcomes the opportunity to lodge a submission to inform the outcomes of the Review of New Zealand's *Civil Aviation Act 1990* (CA Act) and *Airport Authorities Act 1966* (AA Act) (the Review). With the significant changes that have occurred in the global aviation landscape since these pieces of legislation were enacted, Virgin Australia considers the Review is a timely opportunity to assess each Act with a view to enhancing the efficiency and effectiveness of their operation. Like Australia, New Zealand is heavily reliant on aviation for facilitating both economic growth and social connectivity, given its geographic position as an 'end-of-the-line' destination. It is therefore imperative that regulatory arrangements capable of supporting the continued development of New Zealand's aviation sector are in place, underscoring the importance of the Review.

New Zealand is a key market for Virgin Australia. Our first international service in 2004 was operated between Christchurch and Brisbane. Today we operate up to 150 flights per week on 11 routes across the Tasman, serving Auckland, Christchurch, Dunedin, Queenstown and Wellington. We also operate direct services between Auckland and Nuku'alofa, Rarotonga and Apia (as Virgin Samoa). Our strategic alliance with Air New Zealand has enabled us to lift our competitiveness in the trans-Tasman market, delivering a range of benefits for our guests including increased choice, flexibility and convenience for travel between our two countries. Together, Virgin Australia and Air New Zealand operate over 200 flights per week between more than 35 destinations across Australia and more than 25 destinations in New Zealand.

As per advice already provided to the Ministry of Transport, Virgin Australia is in the process of integrating our New Zealand operational base into the rest of our international operations in Australia. This will see us surrender our New Zealand Air Operator's Certificate in March 2014, enabling us to reduce duplication and improve the coordination and efficiency of our international services. From a customer perspective, however, this change will not have any impact on our trans-Tasman operations.

In light of the fact that both the CA Act and the AA Act are fundamentally sound, Virgin Australia has only provided comments below on those aspects of the Review which have the potential to significantly impact our business.

Item D6 – Authorisations of contracts, arrangements and understandings between airlines

Virgin Australia has reviewed alliance partner Air New Zealand's submission in relation to Part 9 (sections 88-91) of the CA Act and is strongly supportive of the views outlined therein. Option 1 (amendment of the CA Act regime) is preferred by Virgin Australia over Option 2 (incorporation of the authorisation process into the *Commerce Act*) based on the reasons provided by Air New Zealand, and as further set out below.

Overall, Virgin Australia does not consider that it is necessary that responsibility for the assessment of the authorisation of arrangements between airlines should be transferred from the Ministry of Transport to the New Zealand Commerce Commission (NZCC). Rather, we support the amendments and improvements to Part 9 outlined by Air New Zealand in its submission. In our view, the potential detriment associated with a complete shift of responsibility to the NZCC outweighs the likely benefits of such a change.

Importance of alliances to Virgin Australia

Development of Virgin Australia's network of alliances is a key pillar of our future growth strategy. Airline alliances are now a standard – and necessary – feature of the global aviation industry. As noted above, Australia is in a similar position to that of New Zealand as an 'end-of-the-line' destination for air services and we do not enjoy direct access to large populations and transit hub traffic as do other more geographically-advantaged regions, such as Asia and the Middle East. Our alliances provide us with a 'capital-light' means of expanding our network and accessing the opportunities in these regions.

Alliances are a critical element of Virgin Australia's ability to offer a product that is competitive. Our capacity to provide our guests with access to extensive networks outside Australia through our alliances with Air New Zealand, Delta Air Lines, Etihad Airways and Singapore Airlines is vital to the long-term sustainability of our business.

Virgin Australia's alliance with Air New Zealand has been a cornerstone of our Game Change Program and will be in the future, consistent with the objectives articulated in the Virgin Vision strategy to drive further growth of our business. The trans-Tasman market is a key element of our service proposition for the corporate and government sector, and without the alliance, we could not match our key competitor's product offering on this route.

It is therefore of significant importance to Virgin Australia that the authorisation function in New Zealand resides with the appropriate regulator.

Regulator choice

Virgin Australia believes that the Ministry of Transport is the appropriate regulatory entity to administer the authorisation process. The value of the Ministry's significant experience in considering airline alliance authorisation applications should not be underestimated.

We note the statement in the consultation document at paragraph 109.4 that moving to a *Commerce Act* and NZCC process would achieve "consistency with the Australian regime".

In our view, this statement fails to take into account key differences between the Australian Competition and Consumer Commission (ACCC) and the NZCC.

The ACCC's scope for investigation under the *Competition and Consumer Act* (CCA) is much broader than the remit of the *Commerce Act*. The ACCC is required to take into account a range of public benefits (and detriments) generated by alliances that reach beyond pure economic principles and there is no requirement that they be quantifiable.¹ In relation to airlines, the key non-economic benefits accepted by the ACCC have included offering guests reciprocal access to partner airline lounges and frequent flyer programmes, the stimulation of tourism and greater availability of connecting flight options.² In contrast, the NZCC's ability to consider these key qualitative benefits appears to be limited as its responsibility is to "quantify benefits and detriments to the extent that it is practicable".³

The NZCC has limited experience dealing with the complex issues inherent in the aviation industry due to the fact that the responsibility is vested in the Ministry of Transport. On this point, Virgin Australia considers that there is significant value in the responsible regulator having a deep understanding of the industry's complexity. It is noteworthy that in many international jurisdictions, primary responsibility for this function resides with the transport ministry, in recognition of the relevance of the specialist expertise relating to the aviation economic regulatory framework and familiarity with the industry held by these regulatory bodies.

Enhancements to the Ministry of Transport's regime

Virgin Australia contends that the efficiency of the Ministry of Transport's regime could be enhanced by implementing a formal framework for assessments, including codification of the criteria that the Ministry currently uses in its consideration and by setting clear timelines for the approval process.

Allowing conditions to be imposed on a grant of authorisation and setting clear timeframes for the process are also changes that would be consistent with the approach taken by the ACCC under the CCA.

Costs

Virgin Australia is of the view that transferring the authorisation regime from the Ministry of Transport to the NZCC would involve significant costs for no real benefit. Currently, applicants are able to assume that the Ministry holds a strong understanding of the airline industry and its nuances, which delivers efficiency benefits and provides us with some certainty about the relevant processes. This is important given that authorisation applications are a routine yet significant process occurring every three to five years.

Virgin Australia is not persuaded that the benefits of the changes proposed by Option 2 are outweighed by the potentially significant detriments involved in a wholesale change of legislation and regulator. We strongly support Option 1 and Air New Zealand's submission in that respect.

¹ ACCC Authorisation Guidelines 2013 at [6.26].

² See for example ACCC, Determination - Applications for authorisation lodged by Virgin Australia Airlines Pty Ltd, Air New Zealand Limited and Others in respect of an airline alliance between the applicants Date: 3 September 2013 Authorisation numbers: A91362 & A91363 at ii.

³ NZCC Final Authorisation Guidelines 24 July 2013 at [49].

Item E1 – Specified airport companies

Virgin Australia strongly supports maintaining the status quo in relation to the definition of 'specified airport company'. We are of the view that it is important that the airports at Auckland, Christchurch, Dunedin, Queenstown and Wellington all continue to remain as specified airport companies and subject to the corresponding regulatory requirements in relation to information disclosure and consultation with substantial customers about certain capital expenditures. In our experience, each of these airports hold substantial market power as monopolistic service providers, and it is therefore appropriate that they continue to be classified as specified airport companies to mitigate against the risk of such airports seeking to extract excessive fees from their customers.

If Option 4 in relation to the adoption of a threshold based on annual passenger movements, (as preferred by the Ministry of Transport) is pursued, Virgin Australia would request that that the specified threshold is lowered to 750,000 passengers per annum in order to incorporate Dunedin Airport. It is essential that Dunedin Airport remains classified as a specified airport company, to ensure that Virgin Australia, as the only airline providing international services to Dunedin, can expect that the airport operator will consult with us in relation to capital expenditures. Aeronautical fees paid to airports represent one of the most significant costs we face as a business. Consultation provides airlines with the opportunity to influence decisions by airport operators regarding proposed capital expenditure, which affects aeronautical fees. Without consultation, airports are not incentivised to make efficient investment decisions, with potentially negative implications for airlines in terms of increased aeronautical charges.

Item E3 – Consultation on certain capital expenditure; Item E4 – Threshold for consultation on certain capital expenditure

Virgin Australia supports the proposal to require all airports to consult with their substantial customers in relation to capital expenditure decisions. This would ensure that if Dunedin Airport was no longer classified as a specified airport company, it would still be required to consult with Virgin Australia in relation to particular proposed capital expenditures.

Virgin Australia does not, however, support the threshold concept for determining whether consultation on capital expenditure should occur. Airport operators incur capital expenditure and in turn seek to recover this cost through increased aeronautical fees charged to airlines. It is our view that any expenditure an airport operator intends to pass on to airlines through increased fees should require consultation. The most transparent approach would be for the airport operator to develop, in consultation with airlines, a capital expenditure program over a three to five year timeframe. The airport operator would then report on progress with capital works and associated expenditure, or discuss with airlines the potential to adjust that expenditure in accordance with the need to prioritise particular projects during the term of the program.

Virgin Australia would envisage that an approved capital expenditure program would include an amount for minor capital projects that could be spent at the discretion of the airport operator. Airline operators would only be required to report on the progress of such projects or activities if funding would exceed the amount agreed under the program.



This suggested alternative to the threshold concept provides airlines with a measure of price certainty, and is closer to the model used by Australia's major airports.

Should you have any queries or wish to discuss any aspect of our submission in further detail, please contact [REDACTED]

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